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IN THE UNITED STATES BANKRUPTCY COURT  
DISTRICT OF OREGON

In re	)	
	)	
ROMAN CATHOLIC ARCHBISHOP OF	)	Case No. 04-37154-elp11
PORTLAND IN OREGON, and	)	
successors, a corporation sole, dba the	)	
ARCHDIOCESE OF PORTLAND IN	)	
OREGON,	)	
Debtor.	)	
_____	)	
TORT CLAIMANTS COMMITTEE,	)	Adv. Proc. No. 04-03292-elp
	)	
Plaintiff,	)	DEBTOR'S BRIEF IN RESPONSE TO
v.	)	THE TORT CLAIMANTS
	)	COMMITTEE'S THIRD MOTION FOR
ROMAN CATHOLIC ARCHBISHOP OF	)	PARTIAL SUMMARY JUDGMENT
PORTLAND IN OREGON, and	)	
successors, a corporation sole, dba the	)	
ARCHDIOCESE OF PORTLAND IN	)	
OREGON, ET AL.	)	
Defendants.	)	
_____	)	

## TABLE OF CONTENTS

<b>I.</b>	<b>INTRODUCTION</b>	<b>1</b>
<b>II.</b>	<b>SECTION 544(a)(3) DOES NOT PERMIT A HYPOTHETICAL BFP TO TAKE TITLE FREE AND CLEAR OF THE PARISHES', HIGH SCHOOL'S, AND TRUST BENEFICIARIES' INTERESTS</b>	<b>1</b>
<b>A.</b>	<b>A Hypothetical BFP Attempting to Purchase Parish or High School Property From the Debtor has Inquiry Notice of the Interests of the Parishes, the High Schools, and the Trust Beneficiaries</b>	<b>1</b>
<b>1.</b>	<b>Oregon has not Abolished Inquiry Notice</b>	<b>1</b>
<b>2.</b>	<b>The Parishes and High Schools' Possession of the Property Provides Constructive Notice</b>	<b>4</b>
<b>3.</b>	<b>The Debtor's Practices Provide Inquiry Notice</b>	<b>5</b>
<b>4.</b>	<b>The Fact That the Debtor is an Ecclesiastical Corporation Sole Provides Inquiry Notice</b>	<b>6</b>
<b>5.</b>	<b>A Hypothetical BFP has a Duty to Inquire Into the Canon Law Requirements for the Sale of Property</b>	<b>7</b>
<b>III.</b>	<b>THE PARISHES, SCHOOLS, PARISHIONERS, STUDENTS, AND OTHERS ARE BENEFICIARIES OF TRUSTS RECOGNIZED UNDER CIVIL LAW</b>	<b>9</b>
<b>A.</b>	<b>Forms of Trust</b>	<b>9</b>
<b>1.</b>	<b>Charitable Trusts</b>	<b>9</b>
<b>2.</b>	<b>Resulting Trusts</b>	<b>9</b>
<b>3.</b>	<b>Express Trusts</b>	<b>10</b>
<b>B.</b>	<b>The Rights of the Beneficiaries Under Certain Trusts are Superior to the Rights of a Trustee in Bankruptcy</b>	<b>11</b>
<b>1.</b>	<b>Resulting Trusts.</b>	<b>11</b>
<b>2.</b>	<b>Charitable Trusts</b>	<b>11</b>
<b>3.</b>	<b>Express Trusts</b>	<b>12</b>

1	C.	Section 544(a)(3) Should not be Read to Permit the Avoidance of a Beneficiary's Interest in Trust Property Where no Transfer by the Debtor Took Place	12
2			
3	IV.	THE RELIGIOUS FREEDOM RESTORATION ACT PRECLUDES THE COURT FROM APPLYING § 544(a)(3) TO CHANGE THE POLITY OF THE ARCHDIOCESE AND THE PARISHES	12
4			
5	A.	When a Federal Statute Burdens the Free Exercise of Religion, the Religious Freedom Restoration Act Exempts the Religious Person or Entity Unless the Statute Advances a Compelling Governmental Interest by the Least Restrictive Means	12
6			
7			
8	B.	RFRA Applies to the Bankruptcy Code	13
9			
10	C.	The Application of § 544(a)(3) to Consolidate the Parishes and Their Property Into the Debtor's Estate Violates RFRA	14
11			
12	1.	Substantial Burden	14
13	2.	Absence of Compelling Governmental Interest	15
14	3.	Least Restrictive Means	16
15	V.	THE FIRST AMENDMENT DOCTRINE OF CHURCH AUTONOMY PRECLUDES THE COURT FROM APPLYING § 544(a)(3) TO MODIFY THE POLITY AND GOVERNANCE OF THE ARCHDIOCESE AND THE EXEMPLAR PARISHES.	16
16			
17	VI.	CONCLUSION	20
18			
19			
20			
21			
22			
23			
24			
25			
26			

## TABLE OF AUTHORITIES

**Cases**

<i>Akins v. Vermast</i> , 150 Or. App. 236, 242, 945 P.2d 640 (Or. App. 1997) .....	3
<i>Allen v. Hendrick</i> , 104 Or. 202, 227 (1922) .....	10
<i>Andrews v. Hochmuth</i> , 253 Or. 313, 316 (1969) .....	10
<i>Beck v. Aichele</i> , 258 Or. 245, 249, 482 P.2d 184 (1971) .....	3
<i>Belt v. Matson</i> , 120 Or. 313, 320-322 (1927) .....	1
<i>Bohlman v. Coffin</i> , 4 Or. 313, 317 (1873) .....	1
<i>Bryce v. Episcopal Church in the Diocese of Colorado</i> , 289 F.3d 648 (10th Cir. 2002) .....	17
<i>Carnes v. Smith</i> , 222 S.E.2d 322 (Ga. 1976) .....	19
<i>Christians v. Evangelical Free Church (In re Young)</i> , 82 F.3d 1407 (8th Cir. 1996), <i>vacated and rem'd</i> 521 U.S. 1114 (1997), <i>reinstated</i> 141 F.3d 854 (8th Cir. 1998) .....	13
<i>Church of Lukumi Babalu Aye v. City of Hialeah</i> , 508 U.S. 520, 537 (1993) .....	15
<i>City of Boerne v. Flores</i> , 521 U.S. 507 (1997) .....	13
<i>Employment Div. v. Smith</i> , 494 U.S. 872 (1990) .....	13
<i>Gonzalez v. Roman Catholic Archbishop of Manila</i> , 280 U.S. 1 (1929) .....	20
<i>Gorzeman v. Thompson</i> , 162 Or. App. 84, 93 (1999) .....	4
<i>Holbrook v. Hendricks' Estate</i> , 175 Or. 159, 169 (1944) .....	10
<i>In re Bishop College</i> , 151 B.R. 394 (Bankr. N.D. Texas 1993) .....	11
<i>In re Estate of Buesing</i> , 240 Or. 399, 406-407, 402 P.2d 98 (1965) .....	10
<i>In re Golden Triangle Capital, Inc.</i> , 171 B.R. 79, 82 (9 <sup>th</sup> Cir. B.A.P. 1994) .....	11
<i>In re Mills Concepts Corp.</i> , 123 B.R. 938 (Bankr. D. Mass. 1991) .....	12
<i>In re Palmer</i> , 1992 Bankr LEXIS 593 (Bankr. C.D. Cal. 1992) .....	12
<i>In re Parkview Hospital</i> , 211 B.R. 619 (Bankr. N.D. Ohio 1997) .....	11
<i>In re Sale Guaranty Corporation</i> , 220 B.R. 660 (9th Cir. B.A.P. 1998) .....	11
<i>In re Seaway Express Corp.</i> , 912 F.2d 1125 (9th Cir. 1990) .....	12
<i>In re Tessier</i> , 190 B.R. 396 (Bankr. D. Mont. 1995) .....	15
<i>In re Torrez</i> , 827 F.2d 1299 (9 <sup>th</sup> Cir. 1987) .....	11
<i>Jones v. Wolf</i> , 443 U.S. 595, 609 (1979) .....	18
<i>Jones v. Wolf</i> , 443 U.S. at 600 .....	19
<i>Kedroff v. St. Nicholas Cathedral</i> , 344 U.S. 94, 116 (1952) .....	17
<i>Kedroff</i> , 344 U.S. at 116 .....	17
<i>Klamath Falls Assembly of God v. State Highway Commission</i> , 255 Or. 211, 465 P.2d 697 (1970) .....	8
<i>Kreshik v. St. Nicholas Cathedral</i> , 363 U.S. 190 (1960) .....	17
<i>Kresik v. St. Nicholas Cathedral</i> , 363 U.S. 190 (1960) .....	18
<i>Mannix v. Purcell</i> , 19 N.E. 572, 584 (Ohio 1888) .....	20
<i>McClure v. Salvation Army</i> , 460 F.2d 553 (5th Cir. 1972) .....	17
<i>McCormick on Evidence</i> , 615, § 254 (2d Ed. 1972) .....	3
<i>Northside Bible Church v. Goodson</i> , 387 F.2d 534 (5th Cir. 1967) .....	18
<i>Order of St. Benedict of New Jersey v. Steinhauer</i> , 234 U.S. 640 (1914) .....	19
<i>Parker v. Newitt</i> , 18 Or. 274, 276 (1890) .....	10
<i>Rogers v. Donovan</i> , 268 Or. 24, 26-27, 518 P.2d 1306 (1974) .....	3
<i>Serbian Eastern Orthodox Diocese v. Milivojevich</i> , 426 U.S. 696, 709 (1976) .....	17
<i>Sherbert v. Verner</i> , 374 U.S. 398 (1963) .....	13

1	<i>Sherbert</i> , 374 U.S. at 406.....	15
2	<i>Stevens v. American Sav. Institution, Inc.</i> , 289 Or. 349, 356 (1980) .....	4
3	<i>United States v. Ballard</i> , 322 U.S. 78 (1944).....	17
4	<i>Unterkircher v. Unterkircher</i> , 183 Or. 583, 591 (1948) .....	10
5	<i>Watson v. Jones</i> .....	18
6	<i>Watson v. Jones</i> , 80 U.S. (13 Wall.) 679 (1871) .....	17
	<i>Watson v. Jones</i> , 80 U.S. 679, 727 (1871).....	17
	<i>Wisconsin v. Yoder</i> , 406 U.S. 205 (1972) .....	13
	<i>Young</i> , 82 F.3d. at 1420.....	16
	<b>Statutes</b>	
7	11 U.S.C. § 541(b) .....	15
8	11 U.S.C. § 541(b)(1) .....	11
9	11 U.S.C. § 541(c)(2) .....	11, 15
10	11 U.S.C. § 541(d) .....	11, 15
11	11 U.S.C. § 544(a)(3) .....	1
12	11 U.S.C. § 548.....	13
13	42 U.S.C. § 2000bb(b)(1) .....	13
14	42 U.S.C. § 2000bb-1.....	14
15	O.R.S. 128.620(3) .....	9
16	O.R.S. § 65.042 .....	9
17	O.R.S. 128.620(2)(b).....	9
18	O.R.S. 128.630 .....	9
19	O.R.S. 65.042 .....	7, 9, 19
20	O.R.S. 65.067 .....	7, 19
21	O.R.S. 65.357(2)(d).....	7, 19
22	O.R.S. 65.377(2)(c).....	7, 19
23	O.R.S. 87.920 .....	2
24	O.R.S. 93.643 .....	2, 3, 4
25	O.R.S. 93.643(1) .....	1, 3
26	O.R.S. Chapter 93.....	1
	Or. Gen'l Laws at 127 § 9.....	7, 19
	Or. Gen'l Laws at 135-36 §§ 2 and 4.....	19
	Religious Liberty and Charitable Donation Protection Act of 1988, Pub.L. No. 105-183, ....	14
	<b>Other Authorities</b>	
	1987 Oregon Laws Chapter 586 .....	3
	Oregon Laws 1987 Chapter 586 .....	1, 2
	Oregon State Bar CLE publication titled " <i>Principles of Oregon Real Estate Law</i> " (OSB CLE	
	1995) provides in Chapter 8, § 8.6.....	2
	<i>Principles of Oregon Real Estate Law</i> (OSB CLE Supp 2003) at § 8.7 .....	4
	<b>Treatises</b>	
	<i>Restatement (Second) of Trusts</i> § 351, cmt. b (1959) .....	9
	<i>Restatement of Trusts</i> , 2d Ed.....	11

1 **I. INTRODUCTION.**

2 The Roman Catholic Archbishop of Portland in Oregon, and successors, a corporation  
3 sole ("Debtor"), submits this response in opposition to the TCC's Third Motion for Partial  
4 Summary Judgment (the "Third Motion"). As more fully set forth below, the Tort Claimants  
5 Committee's ("TCC") Third Motion should be denied.

6 **II. SECTION 544(a)(3) DOES NOT PERMIT A HYPOTHETICAL BFP TO TAKE**  
7 **TITLE FREE AND CLEAR OF THE PARISHES', HIGH SCHOOL'S, AND**  
8 **TRUST BENEFICIARIES' INTERESTS**

9 The TCC's Third Motion under 11 U.S.C. § 544(a)(3) fails unless the bankruptcy trustee,  
10 as a hypothetical purchaser of the Test Parishes' and High School's property from the Debtor,  
11 qualifies as a bona fide purchaser for value under Oregon law. BFP status requires the purchaser  
12 to have neither record notice nor inquiry notice. If the purchaser has either record or inquiry  
13 notice, then the purchaser is not a BFP. Here, any such purchaser would have inquiry notice,  
14 each of which defeats the TCC's § 544(a)(3) motion.

15 **A. A Hypothetical BFP Attempting to Purchase Parish or High School Property**  
16 **From the Debtor has Inquiry Notice of the Interests of the Parishes, the High Schools, and**  
17 **the Trust Beneficiaries.** Inquiry notice has been part of Oregon common law for more than  
18 130 years. *Bohlman v. Coffin*, 4 Or. 313, 317 (1873). Inquiry notice is (according to the way  
19 TCC's witness Newkirk's exhibits describe it), of " ... [a]ny facts, rights, interests, or claims  
20 which are not shown by the public records, but which could be ascertained by an inspection of  
21 the land or by making inquiry of persons in possession thereof". See *Belt v. Matson*, 120 Or.  
22 313, 320-322 (1927).

23 **1. Oregon has not Abolished Inquiry Notice.** The TCC claims that  
24 inquiry notice was abolished by the 1987 enactment of what is now O.R.S. 93.643(1). The TCC  
25 is wrong. O.R.S. 93.643(1) was enacted as part of Oregon Laws 1987 Chapter 586. That whole  
26 chapter only discusses and deals with record notice; it does not mention inquiry notice. In  
addition, all of O.R.S. Chapter 93 only deals with recording. The purpose of Oregon Laws 1987

Chapter 586 is to clarify which real property records a buyer, title company, or lender would have to check on record notice. Chisholm Decl. ¶ 7. It has nothing whatsoever to do with inquiry notice.

The Oregon State Bar CLE publication titled “*Principles of Oregon Real Estate Law*” (OSB CLE 1995) provides in Chapter 8, § 8.6 that:

O.R.S. 93.643 (along with O.R.S. 87.920) could be construed as abolishing inquiry notice. The drafters of O.R.S. 93.643 report no such intention.

**a. Plaintiff’s Own Evidence Recognizes Inquiry Notice.** Plaintiff relies on the August 11, 2005, Affidavit of the chief underwriter at Chicago Title, Malcolm Newkirk. His Affidavit includes copies of recent preliminary title reports on certain of the parcels involved in plaintiff’s Third Motion. Essentially all of those reports contain an exception for: “ ... [a]ny facts, rights, interests, or claims which are not shown by the public records, but which could be ascertained by an inspection of the land or by making inquiry of persons in possession thereof”. (Emphasis added). See, e.g. Newkirk Decl. Exs. 1, p. 2; 2 pp. 2, 8 p.. 2.; Chisholm Decl. ¶ 8. It is that form of inquiry notice—inspection and inquiry--, that very exceptions to the TCC’s witness’s own title reports, on which the Defendants rely.

Oregon title companies insert the inspection and possession exception for inquiry notice in standard title policies. Chisholm Decl. ¶ 8. These exceptions would not be necessary if inquiry notice, other than recording, had been abolished. Obviously, the title companies, that insure title and have the economic risk of being wrong, think inquiry notice is still the law in Oregon. All for good reason. Inquiry notice is still alive and well in Oregon. Chisholm Decl. ¶ 9).

**b. The Statute must be construed to avoid Unreasonable and Absurd Results.** “It is a fundamental canon that

\* \* \* [I]t is the duty of the court in construing a statute to ascertain the intention of the Legislature and to refuse to give literal application to language when to do so would produce ‘an absurd or unreasonable result,’ but, rather, ‘to construe the

1 act, if possible, so that it is a reasonable and workable law and not inconsistent  
2 with the general policy of the Legislature \* \* \*.

3 *Beck v. Aichele*, 258 Or. 245, 249, 482 P.2d 184 (1971) (quoting and citing cases, emphasis  
4 added). Plaintiff's interpretation of O.R.S. 93.643(1) violates that basic canon of statutory  
5 construction and would bring absurd results. The TCC's theory suggests that inquiry notice,  
6 recognized and applied in Oregon for over 130 years, somehow vanished when the legislature in  
7 1987 enacted a new statute governing recording.

8 **c. Basic Rules of Statutory Construction Direct that Inquiry**

9 **Notice was not Abolished.** *Rogers v. Donovan*, 268 Or. 24, 26-27, 518 P.2d 1306 (1974),  
10 instructs, quoting from *McCormick on Evidence*, 615, § 254 (2d Ed. 1972):

11 [W]hen the common law imposes a restriction not mentioned in the statute, the  
12 restriction has been said to govern, unless the circumstances show a legislative  
13 intention to abrogate it.

14 So, too, here. Inquiry notice is a restriction at common law on what a person need do to be a  
15 BFP. Inquiry notice is not mentioned in 1987 Oregon Laws Chapter 586, and the circumstances  
16 do not show a legislative intention to abrogate it. Just the opposite. Thus, the common law  
17 doctrine of inquiry notice lives and survives.

18 **d. The Oregon Courts continue to recognize Inquiry Notice. In**

19 cases with facts arising subsequent to the time that O.R.S. 93.643(1) became law, Oregon courts  
20 have continued to recognize that inquiry notice is still valid. *Akins v. Vermast*, 150 Or. App.  
21 236, 242, 945 P.2d 640 (Or. App. 1997). In *Akins*, a case decided approximately 10 years after  
22 O.R.S. 93.643 became law, and which is based on events that occurred in 1994, the Oregon  
23 Court of Appeals held that inquiry notice is alive and well. In that case, it found that a  
24 lienholder, seeking to invoke BFP status in order to take title free of a subsequently recorded  
25 interest, could not do so because it had a duty to inquire. *Akins* is interesting because it provides  
26 instruction on how even the most obscure fact (a buyer asking to retain \$1,500 of the loan

proceeds after stating he needed the entire \$21,500 to purchase the property) was sufficient to put the lender on notice of the buyer's fraud that would have been discovered on further inquiry. *See also, Gorzeman v. Thompson*, 162 Or. App. 84, 93 (1999).

The 2003 supplement to *Principles of Oregon Real Estate Law* (OSB CLE Supp 2003) at § 8.7 comments:

The court did not discuss O.R.S. 93.643 in the *Akins* or *Gorzeman* opinion. The results suggest that O.R.S. 93.643 bears on the meaning of record notice but not on inquiry notice.

**e. The TCC's Interpretation would Raise Constitutional Issues.**

If the TCC's interpretation were to prevail, a serious constitutional issue would arise on whether the enactment of the 1987 statute violated rights of the parishes and high schools by taking away the property rights they had under inquiry notice prior to enactment of the statute. Also, such a result would raise serious First Amendment and RFRA issues. Statutes should be construed if possible to avoid constitutional issues. Holding that inquiry notice is still alive and well and not abolished by the 1987 legislation would avoid those issues at least relating to inquiry notice.

**2. The Parishes and High Schools' Possession of the Property Provides**

**Inquiry Notice.** Possession of real property by the prior owner, or someone other than the record owner, has long been sufficient inquiry notice to a prospective purchaser. *Stevens v. American Sav. Institution, Inc.*, 289 Or. 349, 356 (1980). The Exemplar Parishes and High School properties consists of parish churches, parish halls, rectories, school buildings, gymnasiums, and athletic fields and structures. Each parish church and school has signs denoting them as such (e.g., St. Brigitta Catholic Church, St. Elizabeth Ann Seton Catholic Church, St. Philip Benizi Catholic Church, Holy Redeemer Catholic School, Regis Catholic High School); Lewis Decl. filed in Support of TCC's Third Motion, Exs. 1 and 2; Bachman Decl. Filed in Support of TCC's Third Motion, Exs. 1-8). None of the churches or schools have signs suggesting any relationship with the Debtor or the Archdiocese of Portland.

If a prospective purchaser were to inspect the parish property the inspection would reveal

1 the property is occupied by the parish priest and the parishioners. If that person were to inquire  
 2 of someone at the parish about buying the property, such prospective purchaser would be  
 3 directed to the pastor. If the purchaser were to first approach the Debtor, the purchaser would be  
 4 referred to the pastor. Wilson Decl. ¶ 7. The Debtor would only become involved once the  
 5 decision had been made at the parish level to sell the property. There is no possible way a person  
 6 could purchase the property directly from the Debtor without the pastor's involvement and  
 7 consent. Wilson Decl., ¶ 7 .

8           **3.     The Debtor's Practices Provide Inquiry Notice.** It would be impossible  
 9 for a BFP to purchase parish or high school property without the Debtor following canonically  
 10 mandated procedures. Wilson Decl., ¶ 7. The Debtor's established practices and procedures to  
 11 accomplish this have been in place for many years. Wilson Decl. ¶ 9. Although Canon Law  
 12 requires the Archbishop's permission, parish property cannot be sold without the consent of the  
 13 pastor, in consultation with the parish advisors. If a prospective buyer were to contact the Debtor  
 14 about purchasing parish property, the buyer would be directed to the pastor. Wilson Decl. ¶¶ 5  
 15 and 7.

16           The pastor, in consultation with the parish advisors determines if the parish wants to sell  
 17 the property, determines the sale price, selects a realtor if one is to be involved, and negotiates  
 18 the commission rate. Purchase offers are presented to the pastor. The pastor, in consultation  
 19 with the parish advisors, decides which offer to accept. Wilson Decl. ¶ 5.

20           The Archdiocesan Property Office coordinates closing the transaction. It provides any  
 21 requested corporate documents to the title company and reviews the closing documents prior to  
 22 submitting them to the Vicar General for signature. The sales proceeds are paid to the Debtor, as  
 23 record title holder, and then disbursed to the parish according to the direction of its pastor.  
 24 Wilson Decl. ¶ 5.

25           Often people dealing with parishes in making bequests or other gifts of real property are  
 26 surprised to learn that the Debtor needs to be involved in the transaction. Wilson Decl. ¶ 8. It is

conceivable that a prospective buyer would have no knowledge of the Debtor's involvement, or that the Debtor held record title, until that information is presented to the buyer on a sale agreement or other transactional document.

Similar procedures would be followed for the sale of Catholic high school properties, the only difference being that the principal and school advisory board would make the decisions rather than the pastor and the parish advisors. Wilson Decl. ¶ 9.

**4. The Fact That the Debtor is an Ecclesiastical Corporation Sole Provides Inquiry Notice.** The fact that the Debtor is an ecclesiastical corporation sole, named "Roman Catholic Archbishop of Portland in Oregon, and successors, a corporation sole," in and of itself, creates a duty of inquiry. The following questions should become apparent to any would-be purchaser of property titled in the name of such corporation: What is a corporation sole? What powers does it possess? Who is the Roman Catholic Archbishop of Portland in Oregon? What does legal title in the name of such a corporation mean? What authority does that corporation have to buy and sell local church property? Does the corporation have a board of directors? If so, does it need the board's approval of the sale? What do the corporation's articles of incorporation say? Is a corporate resolution required? Who has authority to sign a deed on behalf of the corporation? Since the property appears to belong to the parish, do I need to talk to the pastor or someone else at the local church about buying the property? Do the parishioners have any rights or interests? Do they need to be consulted?

An ecclesiastical corporation sole, here being the incorporated office of a Catholic Archbishop, is an oddity in and of itself. Any hypothetical "reasonable prudent person" attempting to purchase property from such a corporation would necessarily have a duty to inquire and obtain answers to questions like those stated above before buying property from that corporation. The record title itself even raises questions which triggers a duty to inquire further.<sup>1</sup>

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<sup>1</sup> See *Newkirk Decl.*, Ex. 21, pg 1: the vestee of one parcel is "Roman Catholic Archbishop of Portland in Oregon and successors, a corporation sole for the benefit of The Immaculate Conception Church"; Ex 1, pg 16-17: vestee is "Archdiocese of Portland By St. Elizabeth Ann Seton"; Ex 5, pg 37: shows "HOLY REDEEMER" on a recorded plat; Ex. 7, pg. 51-52: a recorded document mentioning "the existing building at St. John Fisher School", and a

1 It is unreasonable for a buyer of property from an ecclesiastical corporation sole to look  
 2 only at the vesting deed to confirm that the corporation holds record title to the property. The  
 3 buyer must look at its Articles to see whether there may be restrictions on its ability to convey  
 4 title. The buyer cannot merely accept a deed signed by an authorized representative of such  
 5 corporation, when it is readily apparent that the property is being used as a parish church or  
 6 Catholic high school, and neither the Archbishop nor the corporation sole are in physical  
 7 possession of the property. The parties in possession of and using the property on a day-to-day  
 8 basis are the parish priests, the parishioners, students and others. Any reasonable prudent person  
 9 would begin his or her investigation into purchasing the property at the parish or high school  
 10 itself, not at the county recording office.

11 **5. A Hypothetical BFP has a Duty to Inquire Into the Canon Law**  
 12 **Requirements for the Sale of Property.** The TCC admits that a prospective purchaser would  
 13 have to look at the Oregon statutes and the Debtor's Articles of Incorporation. The TCC  
 14 wrongly suggests, however, that a prospective BFP would be entitled to reasonably conclude,  
 15 solely from reading the Oregon Non-Profit Corporation Act and the Debtor's Articles, that "the  
 16 Debtor has statutory and corporate authority to give clear title to its property, wherever located in  
 17 the Archdiocese." The TCC ignores altogether those multiple portions of Oregon corporation  
 18 law *for religious* corporations that permit the Debtor to govern itself according to Canon Law.  
 19 See Debtor's Combined Brief at 7-12; Or. Gen'l Laws at 127 § 9 (requiring the ecclesiastical  
 20 official who is the corporation sole to act in conformity with church law); O.R.S. 65.067 (same);  
 21 O.R.S. 65.042 (establishing that church law trumps the Oregon Non-Profit Corporation Act when  
 22 the two are in conflict); and O.R.S. 65.357(2)(d) and O.R.S. 65.377(2)(c) (permitting a religious  
 23 corporation's officers and directors to rely upon information from religious authorities in  
 24 managing the corporation).

25 kindergarten and library addition there, and page 54 thereto describes the owner of the parcel as "Archdiocese of  
 26 Portland in Oregon/St. John Fisher Church (Owner)"; Ex 8, pg 5, 12, and 13: contains recorded plats maps showing  
 the parcel as "Queen of Peace Catholic Church"; and Ex 22, pg 8, is a recorded Memorandum of Agreement  
 Affecting Real Property showing Regis High School as the Borrower under an Energy Services Agreement.

1 The TCC likewise ignores those provisions in the Debtor's articles and the supplements to  
2 those articles that limit the Debtor corporation's purposes, powers, and operations to those  
3 consistent with Catholic doctrine, Catholic usages, and Canon Law. Debtor's Combined Brief at  
4 13-14. Just as Archbishop Vlazny vowed to conduct his episcopacy in accordance with Canon  
5 Law when he first became a bishop, the Debtor's articles of incorporation require that the  
6 Archbishop—who, along with his successors, *is the corporation sole*—be appointed into office,  
7 be authorized and empowered to act, be limited in his goals and purposes, and hold and conduct  
8 his office in accordance with Catholic doctrine, Catholic usages, and Canon Law. Debtor's  
9 Combined Brief at 13-14; Declaration of John Vlazny filed herein on Sept. 19, 2005 (hereinafter  
10 Vlazny Decl.) at ¶¶ 2 and 4; Declaration of Thomas W. Stilley filed herein on Sept. 19, 2005  
11 (hereinafter Stilley Decl.) at Ex. 1.  
12

13 The Debtor does not dispute that Oregon law and its own Articles authorize it to convey  
14 property to which it holds record title; however, Oregon law and those same Articles recognize  
15 that the Debtor must comply with religious doctrine and practice in doing so. This is enough to  
16 put a prospective buyer on inquiry notice that it should inquire further into what Catholic  
17 religious doctrine and practice, including Canon Law, requires.

18 In *Klamath Falls Assembly of God v. State Highway Commission*, 255 Or. 211, 465 P.2d  
19 697 (1970) the Oregon Supreme Court held that a buyer of property adjacent to vacant land that  
20 was expected to become a public highway took subject to the minutes of the State Highway  
21 Commission from many years before where those minutes disclosed that there would be no  
22 access to the highway from the property he was buying. The court found notice of this  
23 restriction existed because the deed to the State Highway Commission of the property next door  
24 included the words “for highway purposes”. The court said those three words imposed on the  
25 buyer the duty to inquire further, including looking at “official minutes” of the State Highway  
26 Commission from 1944, which minutes would have notified the buyer that property he was

1 purchasing would not have access to the highway. As that buyer had a duty to inquire further by  
 2 looking as far as those minutes, a prospective buyer of parish or high school property would  
 3 certainly have the duty to further inquire as to what Catholic doctrine, Catholic usages, and  
 4 Canon Law requires.

5 The First Amendment to the United States Constitution, the resulting Church Autonomy  
 6 Doctrine, and O.R.S. 65.042 require that the Debtor be permitted to govern itself and administer  
 7 its affairs in accordance with Canon Law and its own religious practices. See Debtor's  
 8 Combined Brief at pages 3-5, 8-9, and 23-30. In doing so, the Debtor must comply with the  
 9 canons regarding the administration of church property. The canons provide that the pastor, not  
 10 the Archbishop, is the administrator of parish property. The parish pastor, in consultation with  
 11 his own parish advisors, makes the decision whether to sell parish property. Cafardi Decl. ¶ 29.  
 12 If the value of such property exceeds \$516,500, the transaction requires the consent of not only  
 13 the Archbishop, but also the Archdiocesan Finance Council, the College of Consultors, and those  
 14 concerned. Cafardi Second Decl. ¶ 7. The Debtor's established practices regarding the sale of  
 15 property bear this out. See Section II.A.3 above.

### 16 **III. THE PARISHES, SCHOOLS, PARISHIONERS, STUDENTS, AND OTHERS** 17 **ARE BENEFICIARIES OF TRUSTS RECOGNIZED UNDER CIVIL LAW**

18 **A. Forms of Trust.** Oregon law recognizes various forms of trusts. A brief  
 19 summary of some of those that may be applicable here are:

20 **1. Charitable Trusts.** In Oregon a corporation sole "...which has accepted  
 21 property to be used for a particular charitable purpose...", such as for a parish or school, has a  
 22 fiduciary duty to use that property for that particular charitable purpose. O.R.S. 128.620(2)(b),  
 23 O.R.S. 128.630 and O.R.S. 128.620(1) and O.R.S. 128.620(3). No particular words, or even the  
 24 word "trust", are necessary to create a charitable trust. *Restatement (Second) of Trusts* § 351,  
 25 cmt. b (1959). The evidence submitted by each of the defendants, referred to hereby, establishes  
 26 that parish and high school properties are held in charitable trusts.

**2. Resulting Trusts.** Oregon enforces resulting trusts. *Parker v. Newitt*, 18

1 Or. 274, 276 (1890):

2 The principle is well settled in equity that where one purchases an estate and pays  
3 for it and takes the title in the name of another, or where one purchases land with  
4 the money of another and takes the title to himself, there arises, by operation of  
law, a resulting trust in favor of him whose money paid for it.”

5 *Accord: Unterkircher v. Unterkircher*, 183 Or. 583, 591 (1948); *In re Estate of Buesing*,  
6 240 Or. 399, 406-407, 402 P.2d 98 (1965). The evidence submitted by the defendants,  
7 referred to hereby, shows that the parish and high school properties are also held in  
8 resulting trusts.

9 **3. Express Trusts.** As with charitable trusts, express trusts are found and  
10 enforced in Oregon based on all the facts and circumstances. *Allen v. Hendrick*, 104 Or. 202,  
11 227 (1922). In determining whether assets should be subject to a trust under Oregon law, “... the  
12 guiding principle is that the court should give effect to the intent of the person creating the fund  
13 if it is possible to learn from competent evidence what that intent was.” *Andrews v. Hochmuth*,  
14 253 Or. 313, 316 (1969). Where the written evidence is ambiguous, resort may be had to  
15 extrinsic evidence to determine the intent of the parties. *Holbrook v. Hendricks’ Estate*, 175 Or.  
16 159, 169 (1944).

17 Archbishop Power’s letter of December 23, 1981 to Mark O’Donnell (Forbes Decl. ¶ )  
18 provides strong evidence of the existence of a trust for the benefit of the parishes and  
19 parishioners. That letter states:  
20  
21

22 While it is true that the land was transferred to the Archdiocese of Portland, it is  
23 not true that the Archdiocese as such owns the land for itself. The Archdiocese is  
24 an Oregon not for profit corporation incorporated in the state of Oregon, whereas  
the parish is not so incorporated. The title to all property belonging to the Catholic  
25 Church in western Oregon, with some noticeable exceptions such as hospitals,  
nursing homes, private educational institutions, etc., is vested in the Archdiocese.  
Such properties, as for example parish plants, though listed under the  
26 Archdiocesan corporate title, are really held in trust for the individual parishes.

1           **B.     The Rights of the Beneficiaries Under Certain Trusts are Superior to the**  
 2           **Rights of a Trustee in Bankruptcy.** The Bankruptcy Code recognizes that assets held by the  
 3 debtor in trust are not part of the debtor's bankruptcy estate. 11 U.S.C. § 541(b)(1), 11 U.S.C. §  
 4 541(d), 11 U.S.C. § 541(c)(2).

5                   **1.     Resulting Trusts.** In the Ninth Circuit, resulting trusts enforceable under  
 6 state law are enforceable against the trustee in bankruptcy. *In re Sale Guaranty Corporation*,  
 7 220 B.R. 660 (9th Cir. B.A.P. 1998) (holding that a resulting trust good under California law is  
 8 good against the trustee in bankruptcy as a hypothetical BFP under § 544(a)(3) where the trustee  
 9 has inquiry notice of the trust beneficiary's interest). *In re Torrez*, 827 F.2d 1299 (9<sup>th</sup> Cir. 1987)  
 10 (resulting trust imposed for parents on property of debtors as against trustee in bankruptcy where  
 11 parents provided the down payment to purchase property which was titled in the name of the  
 12 debtors, the parents made all the payments on the deed of trust against the property, paid the  
 13 taxes, improved the property, and employed a hired hand to farm the property). *Accord: In re*  
 14 *Golden Triangle Capital, Inc.*, 171 B.R. 79, 82 (9<sup>th</sup> Cir. B.A.P. 1994).

15                   **2.     Charitable Trusts.** Bankruptcy courts enforce charitable trusts against  
 16 claims of trustees in bankruptcy. In *In re Parkview Hospital*, 211 B.R. 619 (Bankr. N.D. Ohio  
 17 1997), the court enforced, against the trustee in bankruptcy, a charitable trust over a restricted  
 18 fund established solely for providing financial assistance to medical students, and containing  
 19 both individual donations made directly to the fund and unrestricted assets placed in the fund by  
 20 the hospital itself. The Court relied primarily on *Restatement of Trusts*, 2d Ed. Similarly, in *In*  
 21 *re Bishop College*, 151 B.R. 394 (Bankr. N.D. Texas 1993) the Court held that the trustee in  
 22 bankruptcy could not reach either the principal or income from two similar trusts established by  
 23 wills leaving to a bank the deceased's property to be liquidated and invested in stocks and bonds  
 24  
 25  
 26

1 with the proceeds to be held in trust for the benefit of the college. Although these cases did not  
 2 involve a bankrupt debtor holding real property in a charitable trust, there is no reason to believe  
 3 that a bankruptcy trustee, attempting to assert the rights of a BFP under § 544(a)(3), would not  
 4 be on inquiry notice (as the trustee is with a resulting trust) regarding parish and high school  
 5 properties which were donated for, and by are being used for, charitable and religious purposes.  
 6

7 **3. Express Trusts.** In *In re Palmer*, 1992 Bankr LEXIS 593 (Bankr. C.D.  
 8 Cal. 1992), the court held that the trustee in bankruptcy under § 544(a)(3) loses to one claiming  
 9 an express trust and whose possession of the property provided constructive notice to any buyer  
 10 of the person's interest in the property.

11 **C. Section 544(a)(3) Should not be Read to Permit the Avoidance of a**  
 12 **Beneficiary's Interest in Trust Property Where no Transfer by the Debtor Took Place.** The  
 13 Ninth Circuit has held that the trustee's rights as a hypothetical BFP apply under § 544(a)(3)  
 14 even where no transfer of the property from the debtor took place. *In re Seaway Express Corp.*,  
 15 912 F.2d 1125 (9th Cir. 1990). The Debtor disagrees with this and asserts that § 544(a)(3)  
 16 should be held to apply only where property has been transferred by the Debtor, following the  
 17 reasoning of cases such as *In re Mills Concepts Corp.*, 123 B.R. 938 (Bankr. D. Mass. 1991). If  
 18 § 544(a)(3) required the existence of a transfer, § 544(a)(3) would be inapplicable here because  
 19 the Debtor did not transfer any of the properties.  
 20

21 **IV. THE RELIGIOUS FREEDOM RESTORATION ACT PRECLUDES THE COURT**  
 22 **FROM APPLYING § 544(a)(3) TO CHANGE THE POLITY OF THE**  
 23 **ARCHDIOCESE AND THE PARISHES.**

24 **A. When a Federal Statute Burdens the Free Exercise of Religion, the Religious**  
 25 **Freedom Restoration Act Exempts the Religious Person or Entity Unless the Statute**  
 26 **Advances a Compelling Governmental Interest by the Least Restrictive Means.** The Free

Exercise Clause of the First Amendment limits government's power to burden the exercise of religion. For decades, the Supreme Court applied a strict scrutiny test when statutes burdened the exercise of religion. In *Sherbert v. Verner*, 374 U.S. 398 (1963), the Supreme Court held that a facially neutral law that burdened the practice of religion must give way to a litigant's free exercise rights unless the government showed that the law furthered a compelling governmental interest by the means least restrictive upon religious liberty. *See also Wisconsin v. Yoder*, 406 U.S. 205 (1972).

In 1990, the Supreme Court limited the circumstances in which the compelling governmental interest test would be applied. *Employment Div. v. Smith*, 494 U.S. 872 (1990). Congress responded by restoring robust protection of religious exercise by enacting the Religious Freedom Restoration Act of 1993 ("RFRA"). RFRA "restore[d] the compelling interest test as set forth in *Sherbert* . . . and . . . *Yoder* . . . and . . . guarantee[d] its application in all cases where free exercise of religion is substantially burdened by government." 42 U.S.C. § 2000bb(b)(1). RFRA is unconstitutional when applied against state law, *City of Boerne v. Flores*, 521 U.S. 507 (1997), but not when applied against federal law.<sup>2</sup>

**B. RFRA Applies to the Bankruptcy Code.** One of the first cases to test the constitutionality of RFRA as applied to federal law involved the interaction between the Bankruptcy Code and religious practices. *Christians v. Evangelical Free Church (In re Young)*, 82 F.3d 1407 (8th Cir. 1996), *vacated and rem'd* 521 U.S. 1114 (1997), *reinstated* 141 F.3d 854 (8th Cir. 1998). In that case, the debtors contributed over \$13,000 to their church in regular tithes the year before they filed their chapter seven petition. The bankruptcy trustee filed an adversary proceeding and invoked 11 U.S.C. § 548 to recover these tithes as preference payments. Even though the Eighth Circuit determined that the tithes were voidable transfers, it

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<sup>2</sup>*Guam v. Guerrero*, 290 F.3d 1210, 1218-21 (9th Cir. 2002); *Christians v. Crystal Evangelical Free Church (In re Young)*, 141 F.3d 854, 858-59 (8th Cir. 1998); *Kikumura v. Hurley*, 242 F.3d 950, 958 (10th Cir. 2001); *Magic Valley Evangelical Free Church, Inc. v. Fitzgerald*, 220 B.R. 386, 393-401 (D. Ct. Idaho 1998); *Mockaitis v. Harclerod*, 104 F.3d 1522, 1530 (9th Cir. 1997); *Sasnett v. Sullivan*, 91 F.3d 1018, 1022 (7th Cir. 1996), *vacated and rem. on other grounds*, 521 U.S. 1114 (1997); *E.E.O.C. v. Catholic Univ. of America*, 83 F.3d 455, 468-70 (D.C. Cir. 1996).

1 refused to order the church to disgorge these sums because RFRA trumped. *Id.* at 1416-20.

2 When Congress amended the Bankruptcy Code's strong arm and avoidance provisions, it  
3 likewise made clear that its amendments--like the Bankruptcy Code itself--were subject to RFRA:

4 Nothing in the amendments made by this Act [amending § 544 and others] is  
5 intended to limit the applicability of the Religious Freedom Restoration Act of  
6 1993.

7 Religious Liberty and Charitable Donation Protection Act of 1988, Pub.L. No. 105-183,  
8 § 6, 112 Stat. 517, 518-19 (June 19, 1998).

9 **C. The Application of § 544(a)(3) to Consolidate the Parishes and Their**

10 **Property Into the Debtor's Estate Violates RFRA.** RFRA's basic rule is that:

11 Government may substantially burden a person's exercise of religion only if it  
12 demonstrates that application of the burden to the person –

- 13 (1) is in the furtherance of compelling governmental interest; and  
14 (2) is the least restrictive means of furthering that compelling governmental  
15 interest.

16 42 U.S.C. § 2000bb-1.

17 **1. Substantial Burden.** Application of Bankruptcy Code § 544(a)(3) to  
18 consolidate parishes and their property into the Debtor's estate would substantially burden the  
19 Archdiocese's exercise of religion because such a result would be contrary to those provisions of  
20 Catholic Doctrine or Canon Law that: (a) establish parishes as separate juridic persons with their  
21 own property; (b) give to parish pastors the authority to administer parish property; (c) require  
22 bishops to conduct their administration and governance in accordance with Canon Law;  
23 (d) require parishes and other juridic persons, when accepting donations for stated purposes like  
24 capital campaigns, to apply those donations exclusively for the intended purposes; (e) require  
25 pastors and bishops to conduct the affairs of their respective parishes and dioceses in accordance  
26 with Canon Law.<sup>3</sup> The TCC's proposed application of § 544(a)(3) would further burden the free

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<sup>3</sup>See generally Debtor's Combined Brief at 16-17, ¶¶ 4-11; Cafardi Decl. at 24-26, 29-31 and its Ex. A., CIC cc. 113-

1 exercise of religion by diverting real estate set aside to advance the ministry of the Church to be  
 2 used to pay tort claimants for claims that arose from the alleged wrongful conduct of an earlier  
 3 generation of Catholic priests and those with authority over them. This could result in the  
 4 closure of parishes and schools and the dispersing of parishioners and families. These burdens  
 5 on religious exercise are vastly more onerous than the recovery of tithes in *Young*.

6 **2. Absence of Compelling Governmental Interest.** As previously  
 7 explained, RFRA restored *Sherbert's* free exercise analysis. When balancing the governmental  
 8 interest, the *Sherbert* Court emphasized:

9 It is basic that no showing merely of a rational relationship to some colorable  
 10 state interest would suffice; in this highly sensitive constitutional area, '(o)nly the  
 11 gravest abuses, endangering paramount [governmental] interest, give occasion for  
 possible limitation,' [of the affected religious exercise].

12 *Sherbert*, 374 U.S. at 406. The purpose of the § 544 (a)(3) strong arm provision, like that of 11  
 13 U.S.C. § 548 in *Young*, is to maximize creditors' recovery. Maximizing creditors' recovery  
 14 cannot be a compelling interest when the Bankruptcy Code itself includes provisions like  
 15 11 U.S.C. § 541(b), 11 U.S.C. § 541(c)(2), and 11 U.S.C. § 541(d) which limit creditors'  
 16 recovery. See *Church of Lukumi Babalu Aye v. City of Hialeah*, 508 U.S. 520, 537 (1993) ("in  
 17 circumstances in which individualized exemptions from a general requirement are available, the  
 18 government 'may not refuse to extend that system to cases of "religious hardship"").

19 Accordingly, *Young* held:

20 We agree with *In re Tessier*, 190 B.R. 396 (Bankr. D. Mont. 1995) that the  
 21 interests advanced by the bankruptcy system are not compelling under RFRA. . .  
 22 [W]e agree that bankruptcy is not comparable to national security or public  
 23 safety. We also agree that allowing debtors to get a fresh start or protecting the  
 24 interests of creditors is not comparable to the collection of revenue through the  
 tax system or the fiscal integrity of the social security system, which have been  
 25 recognized as compelling governmental interests in the face of a religious  
 exercise claim.

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26 116, 373, 393, 515.3, 532, 1256-1257.1, 1267.1, 1267.3, 1279.1, 1282, 1284.2.3; Vlazny Decl. ¶ 9; Second Cafardi  
 Decl. ¶¶ 15-27.

1 *Young*, 82 F.3d. at 1420 (internal citation added). *Young* also recognized that accommodating  
 2 religious exercise as required by RFRA could hardly "undermine the integrity of the bankruptcy  
 3 system as a whole; its effect will necessarily be limited to the debtor's creditors who, as a result,  
 4 will have fewer assets available to apply to the outstanding liability . . ." *Id.* at 1420.

5 **3. Least Restrictive Means.** Even if there were a compelling governmental  
 6 interest, the TCC's proposed application of § 544(a)(3)--like its earlier request that the Court find  
 7 that the parishes are mere operating divisions of an Archdiocesan corporation sole--makes no  
 8 attempt to protect the Archdiocese's free exercise interest by identifying the means least  
 9 restrictive on the religious liberty interest.

10 **V. THE FIRST AMENDMENT DOCTRINE OF CHURCH AUTONOMY**  
 11 **PRECLUDES THE COURT FROM APPLYING § 544(a)(3) TO MODIFY THE**  
 12 **POLITY AND GOVERNANCE OF THE ARCHDIOCESE AND THE**  
 13 **EXEMPLAR PARISHES.**

14 The TCC asks the Court to apply § 544(a)(3) in a manner that would disregard parishes  
 15 as ecclesial entities, strip their pastors of their canonical power to administer parish property,  
 16 collapse those parishes along with their property into the Archdiocesan corporation, and  
 17 eviscerate the Archbishop's authority as canonical steward.<sup>4</sup> Cafardi Decl. ¶¶ 27-31, 35-38, 42.  
 18 The TCC is at the same time requesting the Court to force Regis High School, the Parishes, and  
 19 the Archdiocese to violate the many canonical provisions requiring them as donees to apply the  
 20 gifts they have received in accordance with the donors' purposes or intentions. Cafardi Decl. ¶¶  
 21 8-30.

22 These are core ecclesiastical subject matters off limits to government because the First  
 23 Amendment structurally restrains the Court from becoming entangled in such matters. *Kedroff v.*

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24 <sup>4</sup> The Third Motion ignores the most distinctive facts and issues in this bankruptcy: that the Debtor facilitates the  
 25 temporal affairs of a church; that the Debtor is a particular type of corporation, an ecclesiastical corporation sole;  
 26 that there are six particular, highly relevant provisions in Oregon corporation law that apply to ecclesiastical  
 corporations sole or religious non-profit corporations; that the Debtor's articles of incorporation seven times  
 reference and import Catholic doctrine and usages and Canon Law into the Debtor's governance; that granting the  
 TCC's motion would rewrite the polity and governance of Catholic dioceses and parishes and eviscerate the  
 authority of parish pastors; and that the Religious Freedom Restoration Act and the First Amendment provide  
 additional protections and rights to churches and their civil corporations.

1 *St. Nicholas Cathedral*, 344 U.S. 94, 116 (1952) (identifying "matters of church government" as  
 2 an ecclesiastical subject matter); *Kreshik v. St. Nicholas Cathedral*, 363 U.S. 190 (1960)(same);  
 3 *Watson v. Jones*, 80 U.S. 679, 727 (1871) (identifying "questions of . . . ecclesiastical rule,  
 4 custom or law" as ecclesiastical subject matters); *Serbian Eastern Orthodox Diocese v.*  
 5 *Milivojevich*, 426 U.S. 696, 709 (1976) (identifying "religious law ," "church polity," "control of  
 6 church property," and "structure and administration" of a diocese as ecclesiastical subject  
 7 matters). Debtor's Combined Brief at 23-30.

8 The United States Supreme Court has repeatedly recognized that religious institutions  
 9 determine their own doctrine, polity, and governance.

10 [A] spirit of freedom for religious organizations, an independence from secular  
 11 control or manipulation, in short, power to decide for themselves free from state  
 12 interference, matters of church government as well as those of faith and doctrine  
 13 [and that those organizations] have federal constitutional protection as part of the  
 14 free exercise of religion against state interference.

15 *Kedroff*, 344 U.S. at 116. The Courts, applying these principles of the Church Autonomy  
 16 Doctrine, have refused to apply statutes that would rearrange the polity, governance, or Canon  
 17 Law of a church, *id.*, just as they have refused to apply other statutes touching upon other  
 18 ecclesiastical subjects. *United States v. Ballard*, 322 U.S. 78 (1944) (refusing to apply federal  
 19 mail fraud statute); *McClure v. Salvation Army*, 460 F.2d 553 (5th Cir. 1972) (refusing to apply  
 20 Title VII); *Bryce v. Episcopal Church in the Diocese of Colorado*, 289 F.3d 648 (10th Cir. 2002)  
 21 (refusing to apply 42 U.S.C. §§ 1985 and 1986).

22 In *Kedroff*, the United States Supreme Court voided a New York statute that reallocated  
 23 authority and changed the polity within the Russian Orthodox Church. Invoking *Watson v.*  
 24 *Jones*, 80 U.S. (13 Wall.) 679 (1871), it reasoned:

25 By fiat [the New York legislature] **displaces one church administrator with**  
 26 **another**. It passes the control of matters strictly ecclesiastical from one church  
 authority to another. It thus intrudes for the benefit of one segment of a church

1 the power of the state into the forbidden area of religious freedom contrary to the  
2 principles of the First Amendment.

3 *Id.* at 119 (emphasis added). The TCC's proposed application of § 544(a)(3) would, like  
4 *Kedroff's* New York statute, "displace one church administrator" (the parish pastor) "for another"  
5 (the archbishop). It would also obliterate the distinctive rights and separateness of parishes. The  
6 *Kedroff* Court's conclusion--that "an enactment by a legislature cannot validate action which the  
7 Constitution prohibits . . ."--applies with equal force to the TCC's invocation of § 544(a)(3) to  
8 extinguish parishes as ecclesial entities. *Id.* at 107. *Kedroff* squarely holds that the First  
9 Amendment precludes a legislature from reallocating authority within a denomination. *Id.* See  
10 also *Northside Bible Church v. Goodson*, 387 F.2d 534 (5th Cir. 1967) (invoking *Watson v.*  
11 *Jones* to void the Dumas Act by which the Alabama legislature sought to modify Protestant  
12 denominational polity so that local churches might more easily split off from their  
13 denomination). *Kresik v. St. Nicholas Cathedral*, 363 U.S. 190 (1960) squarely holds that civil  
14 courts may not reallocate authority within a denomination.  
15

16 Indeed, *Jones v. Wolf*, 443 U.S. 595, 609 (1979) itself, immediately after ruling that  
17 neutral principles methodology could be applied in a secessionist church case, abandoned that  
18 approach when it determined the Georgia corporation statute might require it to identify the  
19 transferee on the warranty deed in accordance with church law. It reasoned that "if the Georgia  
20 law provides that the identity of the Vineville church is to be determined according to the 'laws  
21 and regulations' of the [Presbyterian Church in the United States], then the First Amendment  
22 requires that the Georgia Courts give deference to the presbyterial commission's determination of  
23 that church's identity." *Id.* Six separate provisions of the Oregon corporation statutes similarly  
24 require civil authorities to defer to church law so that churches might govern themselves in  
25  
26

1 accordance with their own beliefs.

2 By identifying *Carnes v. Smith*, 222 S.E.2d 322 (Ga. 1976) as an exemplar case for  
 3 resolving a church property dispute, *see Jones v. Wolf*, 443 U.S. at 600, the Supreme Court  
 4 recognized that a church's authority to define its own polity is so great that church law regarding  
 5 property ownership controls even when it produces an opposite result from merely looking to the  
 6 named transferee on a deed. The TCC's bona fide purchaser argument based on § 544(a)(3) is, of  
 7 course, the TCC's latest effort to cause the Court to ignore all contrary law and evidence and  
 8 merely look to the identification of the transferees on the deeds for parish property. *Carnes* and  
 9 *Jones v. Wolf* vindicate the First Amendment principle that churches and denominations get to  
 10 define their own polity, even when the warranty deeds by which they take property may be  
 11 confusing under other civil legal principles.

12  
 13 A fundamental rule of Church Autonomy law is that church law matters because, in  
 14 America, churches get to define their own governance, their own polity, and their own beliefs.  
 15 The Georgia corporation statute cannot change this rule and neither can § 544(a)(3) of the  
 16 Bankruptcy Code. This is why the Oregon corporation law, again and again, expressly defers to  
 17 church law for church corporations. Or. Gen'l Laws at 127 § 9; Or. Gen'l Laws at 135-36 §§ 2  
 18 and 4; O.R.S. 65.067, O.R.S. 65.042, O.R.S. 65.357(2)(d), and O.R.S. 65.377(2)(c). It is why the  
 19 Debtor stated in its articles of incorporation that it would be governed by its own Canon Law. It  
 20 is why the Supreme Court placed ownership of Father Steinhauser's copyrights and copyright  
 21 income after his death in his Benedictine monastery instead of Father Steinhauser's estate even  
 22 though he held the copyrights in his own name. *Order of St. Benedict of New Jersey v.*  
 23 *Steinhauser*, 234 U.S. 640 (1914). It is why Justice Brandeis ruled that Raul Gonzalez could not  
 24 be made a chaplain and could not receive the trust income from his great, great, great,

1 grandmother's trust even though the trust document appeared to require the same. *Gonzalez v.*  
 2 *Roman Catholic Archbishop of Manila*, 280 U.S. 1 (1929). It is why the Ohio Supreme Court  
 3 held that Archbishop's Purcell's assignment for the benefit of creditors which automatically  
 4 transferred all of his property to the trustee in insolvency had no effect on the parish property he  
 5 held in his own name. *Mannix v. Purcell*, 19 N.E. 572, 584 (Ohio 1888). It why the Court here  
 6 must reject the TCC's argument, based on § 544(a)(3), and hold, just as the Ohio Supreme Court  
 7 did, that "[t]he legal title to all this property is in the bishop, while the equitable or beneficial  
 8 interest is in the several congregations . . . ." *Id.* at 590.

## 10 VI. CONCLUSION

11 For the reasons stated herein and as permitted or required by Oregon corporation and  
 12 trust law, the Debtor's articles of incorporation, RFRA, and the First Amendment Doctrine of  
 13 Church Autonomy, the Debtor respectfully requests that the Court deny the TCC's Third Motion  
 14 for Partial Summary Judgment.

16 SUSSMAN SHANK LLP

17 /s/ Thomas W. Stilley

18 By: \_\_\_\_\_  
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25 F:\CLIENTS\14961\004\ADVERSARY PROCEEDING (3RD MOTION FOR PARTIAL SUMMARY JUDGMENT)\P-BRIEF (FINAL FORM).DOC  
 26

CERTIFICATE OF SERVICE

I certify that on October 19, 2005, I served **by first class mail**, a full and correct copy of the foregoing **DEBTOR'S BRIEF IN RESPONSE TO THE TORT CLAIMANTS COMMITTEE'S THIRD MOTION FOR PARTIAL SUMMARY JUDGMENT** to the interested parties of record, addressed as follows:

PLEASE SEE ATTACHED LIST OF INTERESTED PARTIES

Dated: October 19, 2005

*/s/ Thomas W. Stilley*

---

Thomas W. Stilley, OSB No. 88316  
Howard M. Levine, OSB No. 80073  
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